FEDERAL RESERVE BANK OF NEW YORK

ANNUAL REPORT 1987

FEDERAL RESERVE BANK OF NEW YORK

May 13, 1988

TO: Depository Institutions
in the Second Federal Reserve District

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stress that continuing progress in managing and ultimately resolving the debt problems of the developing world rests crucially on the maintenance of an environment in which the "community of interest" among all parties to the process must be preserved and enhanced.

I hope you will find this historical overview of the debt problem of value and interest.

E. Gerald Corrigan
President

Federal Reserve Bank

of New York

SEVENTY-THIRD ANNUAL REPORT

For the Year

Ended

December 31, 1987

Second Federal Reserve District

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Seventy-third Annual Report
Federal Reserve Bank of New York

A PERSPECTIVE ON THE DEBT CRISIS, 1982-87

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In 1982, the onset of widespread payments disruptions ended a period of heavy lending to developing countries (LDCs) and signaled the beginning of the debt crisis. International bankers and policymakers faced a threat of financial disorder on a global scale not seen since the Depression. The response that evolved to address the crisis was deeply rooted in commonly accepted principles of financial relations that have governed the postwar period: international cooperation, official liquidity support, commitment to free trade and world economic growth, and a combination of conditional finance and debtor country adjustment with multilateral oversight. The process of managing the debt problem has been flexible and tailored on a case-by-case basis to circumstances in individual countries. At the same time, it requires a long-term commitment to cooperate by all key parties that has at times been hard to achieve.

From early on, the management of the debt crisis has been criticized in many ways. Some have felt that creditors should be forced to accept losses or grant debt relief; others that exposures should be assumed by multilateral agencies. In the past year or

so, criticisms have grown louder. Highly visible developments such as the Brazilian moratorium on interest payments, extensive additions to loan-loss reserves by international banks, declines in the secondary market prices for LDC debts, and a new proposal for refinancing part of Mexico's bank debt have all worked to intensify interest in the process of managing the debt crisis. Much of the recent commentary has had a pessimistic tone. To assess properly how the process is working, however, it is necessary to step back from the daily headlines and look at developments from a longer term perspective.

The process of managing the debt problem has two major and interrelated long-term goals: (1) to improve LDC economic and financial performance with a view toward sustaining economic growth and, over time, restoring the creditworthiness of individual debtor countries and (2) to reduce the vulnerability of the international banking system to risk on LDC loans. Progress has been made toward reaching both objectives, but at different rates (Chart 1).

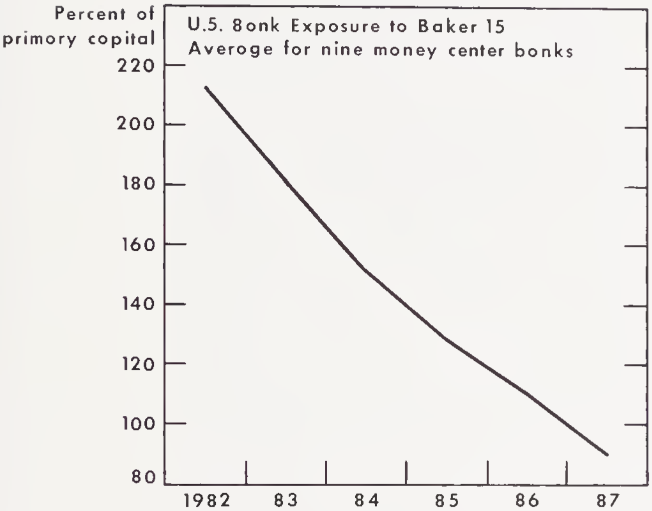
Most positively, banking system exposure relative to capital has declined rapidly. For example, from the end of 1982 to the end of 1987, the exposure of nine U.S. money center banks to a group of heavily indebted developing countries, the so-called Baker 15,* fell from 212 percent of primary capital to 90 percent. Comparable or even larger declines took place for other classes of banks as well. These reductions exceeded expectations held in the early stages of the debt crisis. The declines in exposure ratios resulted in large measure from the efforts of banks, spurred by regulatory concern, to broaden their capital base as well as from a careful management of their creditor positions. In the more recent past, innovations in financing agreements between individual debtors and creditors have contributed to a continued lowering of outstanding exposures. In some cases, however, these reductions in exposure have weakened the commitment of some small banks and some larger regional banks to the process of debt rescheduling and LDC lending. This, in turn, complicated negotiations and sometimes led to long delays in putting together financing.

Progress toward the second and more fundamental goal of restoring LDC creditworthiness has been somewhat of a struggle. Yet, more has been achieved in this regard than is widely perceived and in some cases—notably Colombia and Chile—progress has been rather striking. On balance, however, measures of LDC financial health have shown a mixed picture since the debt crisis started. For example, most relative measures of external debt and debt-service requirements have not improved, in part because of

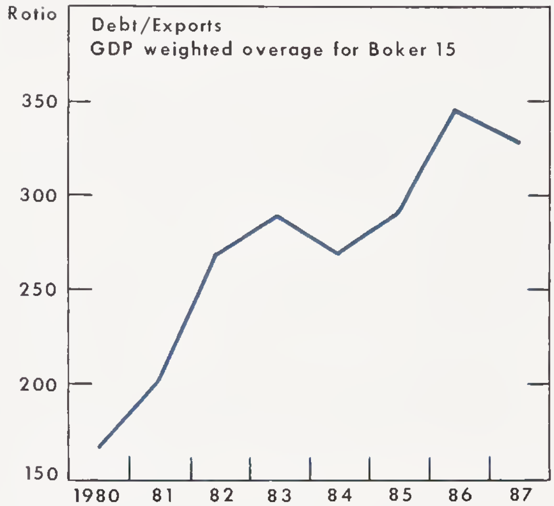
* The Baker 15, so named because they were singled out by Treasury Secretary Baker in his October 1985 debt initiative, will be the principal reference group cited in this essay. Basically, the group comprises the major debtor countries of the developing world: Argentina, Bolivia, Brazil, Chile, Colombia, Cote d'Ivoire, Ecuador, Mexico, Morocco, Nigeria, Peru, the Philippines, Uruguay, Venezuela, and Yugoslavia.

Chart 1. **DEBT STRATEGY OBJECTIVES**

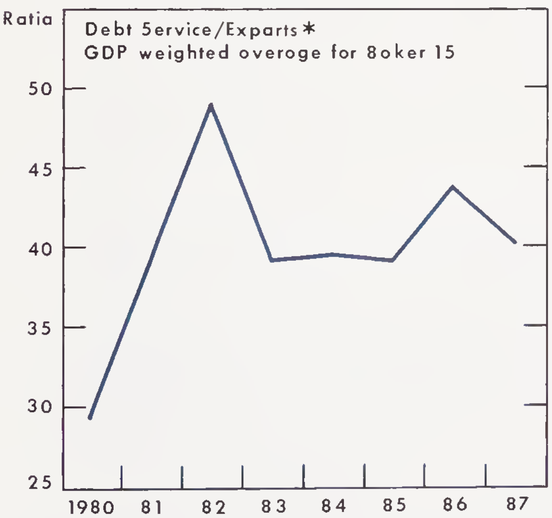
Progress in meeting debt strategy objectives has diverged somewhat. While bank exposure has fallen dramatically . . .



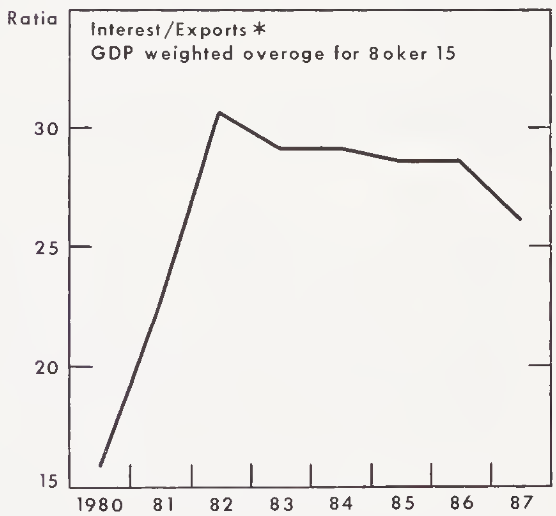
. . . LDC financial measures are mixed. Debt ratios rose on balance since the crisis began . . .



. . . but reschedulings steadied the debt service burden . . .



. . . and interest coverage is generally better.



* Includes adjustments for estimated arrearages in 1986 and 1987.

Sources: IMF, Federal Reserve Bank of New York.

limited growth and adverse trends in the terms of trade.

Although debt burdens remain relatively heavy, the proportion of short-term debt to total debt has fallen sharply for the Baker 15 since the onset of the crisis, from 21 percent in 1982 to 8 percent in 1987, owing largely to reschedulings. This lengthening of the maturity structure of LDC debt has provided many debtors with a more manageable stream of debt-service payments. In addition, interest costs on the debt relative to exports have declined. For the Baker 15, this ratio fell from 31 percent to 26 percent between 1982 and 1987.

Continued efforts to reach the more basic goals of sustained growth and restored creditworthiness are needed. In recent years, the heavily indebted countries have been able, after a long and deep recession, to maintain fast enough economic growth to yield gains in real per capita income, although these gains have been well below the $3^1/_2$ percent per capita growth that they achieved in the past. Moreover, no major developing country that rescheduled its debts since the start of the crisis has been able to restore dependable access to world credit markets, even though the financial condition of a number of the Baker 15 countries has improved. In short, while important progress has been made over the past several years toward the long-term goals of managing the debt problem, major challenges still lie ahead.

The Community of Interests

From the outset, the official community chose to play an active role in LDC payments difficulties rather than leave debtors and creditors on their own. Official representatives, particularly the Managing Director of the IMF and the Chairman of the Federal Reserve, stressed the community of interests all parties had in containing and resolving the crisis.

The goal of creditor governments, private creditors, and the international financial institutions was an orderly restoration of debt service. Over the longer term, official actions aimed to promote economic recovery in developing countries and to restore their normal access to the international financial markets. The IMF helped the process along, encouraging all participants to act responsibly and playing its traditional role as economic advisor and provider of short-term balance-of-payments finance.

The responsibilities of the borrowing countries were to change their economic policies

to reduce internal and external imbalances and to maintain their debt servicing. Policy goals involved, among other actions, keeping exchange rates competitive so as to encourage import substitution and export growth, reducing fiscal deficits, ending subsidies on many domestic goods, and achieving positive real interest rates. Export expansion was viewed as the key to an improved current account position and a reduced debt burden in the long run.

The creditors, too, had their responsibilities. Commercial banks, of course, had the key role of providing appropriate amounts of new funding if countries carried out their adjustment programs. Creditor governments had to arrange reschedulings of their own claims on debtors and support the banks' rescheduling efforts. In a few cases, until an IMF program was approved and a borrowing plan agreed upon, governments provided short-term bridge financing to tide a debtor country over. Such funds, frequently arranged under the auspices of the Bank for International Settlements, played a very important role both in providing limited amounts of short-term official finance and in signaling the willingness of the industrial countries to support the overall process.

This cooperative structure worked well in the immediate wake of the crisis. Over subsequent years, however, the community of interests has, at times, been difficult to maintain. The debtor countries found that implementing stabilization programs was often politically and economically difficult. In some of the Baker Plan countries, newly elected democratic governments were coming into power after long stretches of non-democratic rule. Not surprisingly, these governments faced enormous challenges in seeking simultaneously to solidify democratic institutions while coping with the debt problem. Many countries found it difficult to sustain the kinds of policies needed to meet performance criteria and, consequently, to obtain conditional IMF resources. The IMF attempted to deal flexibly with these difficulties in administering its programs. Where the overall thrust of a country's adjustment effort was satisfactory, the Fund was willing to grant waivers on certain performance targets. Despite that stance, however, some debtor countries grew ever more cautious regarding relationships with the Fund.

Banks worldwide became increasingly frustrated by recurring negotiations and the growing reluctance of smaller, less-exposed banks to take part in new money arrangements. Differences in accounting rules, tax policies, and regulatory practices among creditor countries also contributed to differences in the attitudes of some banks to the process.

Concern about progress on international debt problems was growing in October 1985 when Treasury Secretary Baker put forward his debt initiative. It stressed the need for new financial resources from banks and called on the World Bank, in particular, to add to its flows. These were all familiar themes. The new feature in Secretary Baker's plan was an emphasis on growth-oriented adjustment policies rather than a principal reliance

on macroeconomic stabilization and demand restraint. These structural adjustment policies are broad-ranging: they encompass trade liberalization, such as reduced tariffs and quotas; financial liberalization, such as expanded access for foreign direct investors; deregulation, including eliminating subsidies, rationalizing exchange rate regimes, and removing interest rate controls; and privatization of public sector enterprises.

Progress has been made in following up on the Baker initiative, but it has often been overlooked by focusing on difficulties. The kinds of economic and structural reform policies called for require a demanding long-term commitment, and success among the debtor countries in implementing such steps has been uneven. In some cases, external economic changes, such as commodity price declines, have complicated stabilization efforts. On the financing side, also, some difficulties emerged. Longer delays in getting agreement on bank lending packages worked to slow the overall pace of bank lending. In addition, international banks, first abroad and later in the United States, increased their reserves against possible losses on their LDC loans. These developments, together with renewed financial and economic troubles in some of the major debtor countries, underscored the difficulties in sustaining the broad-based cooperative and complementary efforts needed ultimately to solve the debt problem.

Perceptions about how the debt problem is working out, though, have been overly affected by dramatic events like the Brazilian moratorium. Important, but less dramatic, positive steps have been widely overlooked. Some debtor countries, like Mexico, have made impressive strides in diversifying their export base; others, like Chile, have expanded the array of investments open to capital from abroad. In addition, innovations worked into recent reschedulings and new money packages have provided mutual benefits of greater financial flexibility and hold great potential for the future.

SETTING THE PATTERN: THE RESPONSE TO MEXICO'S CRISIS

The reaction to the Mexican payments shock of August 1982 established a framework for providing emergency liquidity, structuring bank finance, and making IMF oversight and support of adjustment efforts the centerpiece of the process. These became key

features of managing the initial phase of the LDC debt crisis and they worked with notable success in the years just following its onset.

The August 1982 Shock

Mexico's payments difficulties surfaced against a worsening economic environment for the country: in the summer of 1982, the industrial countries were in the midst of a recession; real interest rates had turned sharply positive; and prices of commodities, including oil, were declining. Mexico's payments problem stemmed from a marked decline in its current account balance, combined with massive bouts of capital flight. To finance its external deficits, the country increased its foreign borrowings and drew down reserves. As a result, external debt mushroomed, reaching almost $80 billion by the end of 1981, equal to 2$^{1}/_{2}$ times the country's export earnings. Moreover, as the current account worsened, banks extended credit at shorter maturities, so that by 1982 close to one-third of Mexican external debt was due within a year.

Emergency Liquidity Assistance

Mexico's immediate need in the summer of 1982 was for liquidity. In response to that need, the United States and other governments acted promptly to mobilize financial support for the country. A special meeting of the central banks of the Group of Ten (G-10) countries was held the week following Mexico's August 12 announcement of its debt-servicing problem. The meeting led later in the month to a financial package for Mexico of $1.85 billion. This money was to serve as a bridge to funds that would be forthcoming from the IMF once a program was in place. Of the $1.85 billion package, the United States provided $925 million, other G-10 countries contributed another $750 million, and Spain added $175 million.

Rapid agreement was also reached between Mexico and the U.S. government on other forms of financing. There had already been discussions within the Treasury as to the merit of buying Mexican oil for the U.S. strategic reserves were Mexico to face a payments crisis. Accordingly, the Exchange Stablization Fund of the Treasury provided the Bank of Mexico with $1 billion in a short-term swap arrangement, enabling Mexico to meet immediate payments needs. These drawings were quickly repaid with the proceeds from an advance payment on oil purchases by the Department of Energy.

The immediate reaction to Mexico's financial plight clarified a very important point: namely, that arrangements for providing liquidity support on an international level work well. Speed and creativity were hallmarks of the response to the crisis. To this day the Mexican shock of August 1982 represents the biggest liquidity emergency of an international nature that officials have faced, and the success in dealing with it underscores the usefulness of the current informal understandings among central banks and their governments. The essence of the debt crisis for Mexico and other LDCs, however, lay not just in dealing with a short-term liquidity emergency but also in managing the long-term payments problem. For that, a more structured approach was necessary.

Structuring Bank Finance

The structure that evolved in the Mexican case set a pattern for troubled LDC debtors on key features of commercial bank finance: the advisory committee format, concerted lending, the mutual interdependence of bank lending and Fund programs, and the treatment of other private credits.

In the Mexican case, great efforts were made to draw as many banks as possible into agreement. An advisory committee was set up to contact the hundreds of banks worldwide with Mexican debt and to engage them in a financing package for the country. The most significant step, however, was the initiative of the Managing Director of the IMF, who told the banks that they would have to provide Mexico with new money as a condition for his recommending approval of Mexico's program.

This was a sharp adjustment in the way the Fund normally did business. Typically, an IMF program was negotiated on the basis of assumptions about the volume of private capital inflows. With a Fund agreement in hand, a debtor country could then work out arrangements with its lenders. But because the threat of slippage in the Mexican case was so great, the Fund had to raise the cost of noncooperation. Because the banks would not usually commit any new loans until an adjustment plan was agreed to, the move set up a strong mutual dependence between IMF programs and new money packages. The success of this tactic in the Mexican case created a powerful precedent.

Initially, the banks were taken aback by the Managing Director's announcement. However, the Chairman of the Federal Reserve, who had been working closely with the Managing Director throughout the crisis, stressed that, "in such cases where new loans facilitate the adjustment process and enable countries to strengthen their economies and service their international debt in an orderly manner, new credits should not be

subject to supervisory criticism." This succinctly stated the core of supervisory policy for dealing with the early phase of the debt crisis. In effect, Chairman Volcker was saying that regulators recognized that new bank lending associated with an IMF-supported adjustment program could improve the value of outstanding bank loans. Regulators would not take special supervisory initiatives regarding such new money packages in a context in which a country remained current on its interest obligations. This statement provided reassurance to the banks on new conditional lending. Of course, for reasons including, but not limited to, the LDC debt crisis, bank regulators were consistent in their call for strengthened bank capital positions.

As to which debt to include in the rescheduling, Mexico and its bank creditors quickly agreed that government bonds would continue to be serviced on their original maturity schedule. The bond debt could be easily excluded from the rescheduling because it was of small size. Also, it would have been much more difficult to arrange reschedulings with a relatively large number of widely dispersed bondholders than with banks.

While no one disagreed that debt owed to banks by the government or its agencies would be rescheduled, Mexican private sector debt to international banks was another matter. In Mexico's case, exchange controls had been put in place at the end of the summer to stem the outflow of dollars, making it difficult even for profitable companies to obtain the foreign exchange needed to service their external debt. To meet this problem, the Mexican government called on private sector debtors to reschedule their own debt on an individual basis. In return for peso payments by the private sector debtors, the central bank agreed to provide foreign exchange to service the rescheduled debt in line with an agreed maturity schedule. This scheme basically resulted in the Mexican government taking on the future foreign-exchange risk but not the credit risk of its private sector debtors.

Another pressing problem concerned the placements with Mexican banks in the interbank markets in London and New York. These amounted to some $6.5 billion, of which about 90 percent was due within six months. Unless rollovers could be arranged, all the emergency funds Mexico was putting together could have leaked out through the interbank market. Freezing the deposits at the branches outside Mexico, it was feared, could trigger a disruption in the dollar interbank market. Through their global network, banks on the advisory committee together with Mexican officials pressed lenders to roll over their placements. As a result, there were no serious leakages in these initial months.

Loans to the private sector and interbank placements were not formally included in the rescheduling process. But in practice both were subject to risks similar to those on loans to the public sector. This was a theme that would echo through the debt crisis

generally. For example, the arrangements for the Brazilian rescheduling early in 1983 would require explicit standstill conditions for interbank positions with the offshore branches of Brazilian banks. That action created much consternation among banks for it made clear that international interbank deposits bore country risk. In the case of Chile, where term debt owed by the private sector accounted for close to 50 percent of the country's total external debt, bank creditors pressured the government to take more direct responsibility for the performance of private sector obligations when these ran into trouble. Ultimately, the Chilean government agreed to assume the debts of Chilean banks, but not of other private firms.

The Mexican case laid down a basic pattern for handling bank loans to LDCs:

- Loans to governments of all bank creditors worldwide were rescheduled under terms negotiated through the advisory committee. Banks rescheduled near-term obligations only, typically those for the current year and the succeeding year. Later multiyear rescheduling agreements (MYRAs) would be lined up for some of the prominent debtors after periods of good performance. MYRAs aimed to smooth the profile of scheduled amortizations and often called for special monitoring procedures once the rescheduling country was no longer using Fund resources.

- Spreads and fees on the reschedulings as well as the new money packages were initially set rather high compared to pre-crisis levels. For example, in the Mexican case, rescheduled loans carried a 1 percent fee and either $1^{3}/_{4}$ percent over the U.S. prime rate or $1^{7}/_{8}$ percent over LIBOR. Mexico had been paying less on average before the crisis hit. For other countries rescheduling costs would be comparable.

- Interbank lines and private sector loans were clearly subject to country risk, but were not formally included in reschedulings in the same way as loans to governments. Only bond debt was specifically excluded from debt-servicing interruptions. This was of little benefit to LDCs, however. Although securities were a *de facto* senior obligation to bank debt, the bond market was not open as a source of new money to debtor countries.

- Bank packages, official reschedulings, and IMF agreements were linked. This put pressure on reluctant creditors and promoted more rapid arrangements. It would emerge later, however, that even conditioning Fund programs on setting up the bank packages first would not be enough to overcome the friction caused by

requiring the active support of some banks. Marginal creditors had little to lose from taking a hard line and could hope to escape entirely from any new money commitments by not cooperating. Over time the need to consolidate creditor positions in order to get a more efficient bargaining process would become pressing.

SOME EARLY SUCCESS

Within a year and a half of Mexico's difficulties, some 26 developing countries worldwide rescheduled over $50 billion in debt with their private and official creditors and adopted economic stabilization programs. Although financial problems were widespread, most debtor countries addressed them in a cooperative way and seemed to be grappling effectively with their economies in a favorable world environment. The volume of world trade rebounded, expanding 3 percent in 1983 and almost 9 percent in 1984. Inflationary pressures were contained and interest rates declined. Moreover, recovery in the industrial world strengthened the prices for non-oil commodities in dollar terms, halting the downturn in the Baker 15 terms of trade by 1984 (Chart 2).

In the early years of the crisis, neither debtors nor creditors doubted that the LDCs would have to adopt some tough measures to reduce their external deficits and borrowing needs. Although banks had provided LDCs a substantial amount of funds through concerted lending arrangements in 1983—almost $13 billion to the Baker 15—it was clear that new bank lending would not come easily despite the obvious interests of the banks in supporting the overall process. Strong economic policies were needed, not only to reduce imbalances but also to maintain access to bank and Fund monies. Stabilization efforts required disciplined monetary policies, competitive exchange rates, positive real interest rates and noninflationary wage policies, as well as reductions in government budget deficits through spending restraint, reduced subsidies, and increased taxes. The goal of the programs was basically to reduce domestic demand and raise the prices for tradable goods. By this means, exports would rise, imports would fall through both income and price changes, and the external deficit would decline.

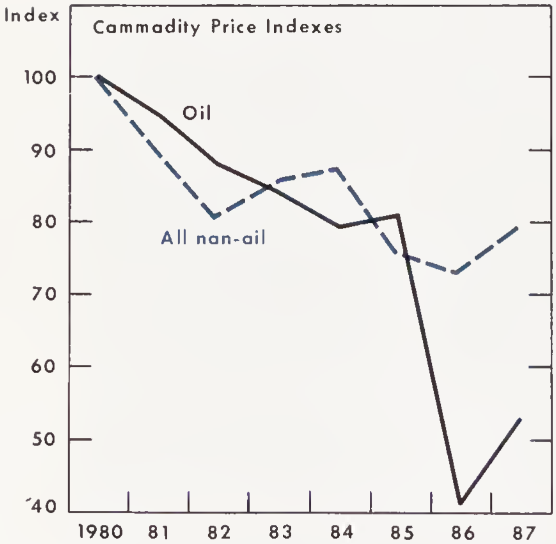
Retrenchment was the necessary first stage of adjustment; indeed, debtor countries would likely have had to restrain demand more if the IMF had not been overseeing the process. But macroeconomic stabilization alone could not serve as a complete long-

Chart 2. **THE ECONOMIC ENVIRONMENT**

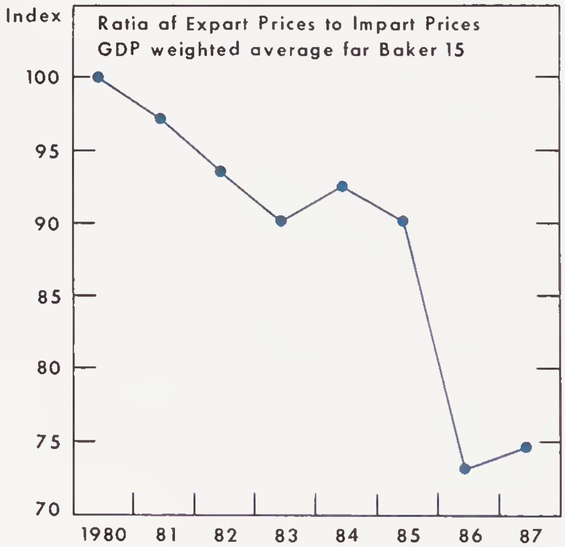
Key features of the global economy turned out favorably for LDC financial prospects . . .

	Expected Change for 1983-87 under "Moderately Optimistic" Scenario for LDC Recovery *	Actual Change 1983-87
OECD growth Average annual percentage change	**3.0**	**3.3**
OECD inflation Average annual percentage change	**5.0**	**4.1**
Interest rates Cumulative basis point change in six-month LIBOR	**–200**	**–187**

. . . but weak commodity prices . . .



. . . led to worsening terms of trade that disrupted chances for recovery.



* From Ronald Leven and David Roberts, "Latin America's Prospects for Recovery," Federal Reserve Bank of New York Quarterly Review, Autumn 1983.

Sources: OECD, IMF, Federal Reserve Bank of New York.

term policy. The hope was that strong steps in the early phase of adjustment would make a significant contribution to restoring debtor country creditworthiness. Over the longer run, it was clear that emphasis would have to be put on tackling the hard problem of structural reform.

That strategy seemed to be yielding gains, as countries began to put their policies in place. In 1983, the Baker 15 countries cut their combined current account deficit by two-thirds from its 1982 level. They reduced the deficit to near-balance in 1984 from almost $51 billion two years earlier (Chart 3). In large part, the 1983 successes in external performance resulted not from strong growth in exports, whose volume increases were offset by price declines, but from declines in imports. Import volumes for the Baker 15 fell 21 percent in 1983; further reductions were made the next year.

By 1984, many of the Baker Plan countries were able to report renewed export growth, spurred in part by the lagged results of earlier exchange rate depreciation. Strong external performance in these years was also aided by improvements in some commodity prices, such as those for agricultural raw materials, food, and beverages. But recovery in the industrial world helped the most. The value of U.S. imports from the Baker 15 increased by 14 percent in 1984 over their 1982 level.

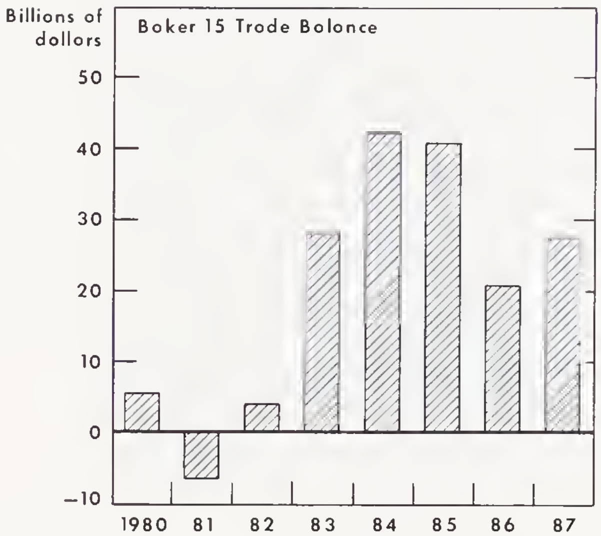
Adjustments in the Major Debtor Countries

The relative optimism about the working of the debt strategy in the initial years of the crisis was prompted largely by the successes of Mexico and Brazil. In Mexico, the new government of President de la Madrid vigorously implemented a series of important policy initiatives. Subsidies on food and utilities were cut, public sector expenditures were reduced, and the real exchange rate was sharply devalued. Exchange controls were gradually eased, and by the end of 1983, interest arrears on private sector debt had been eliminated. The country met its government deficit target in 1983 but somewhat overshot the 1984 goal of 5.5 percent of GDP.

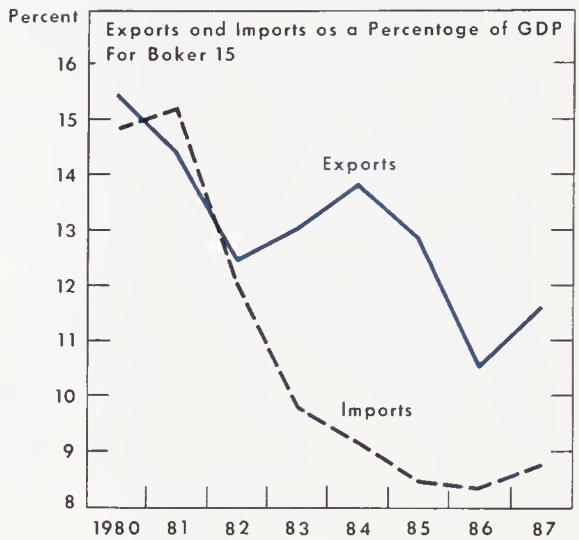
Mexico had some early success reducing the rate of inflation, from close to 100 percent in 1982 to 59 percent in 1984; but by year-end 1984, the country was still above its target of a 40 percent inflation rate. Moreover, Mexico was able to record positive real interest rates only intermittently during those early years.

Chart 3. LDC EXTERNAL ACCOUNTS

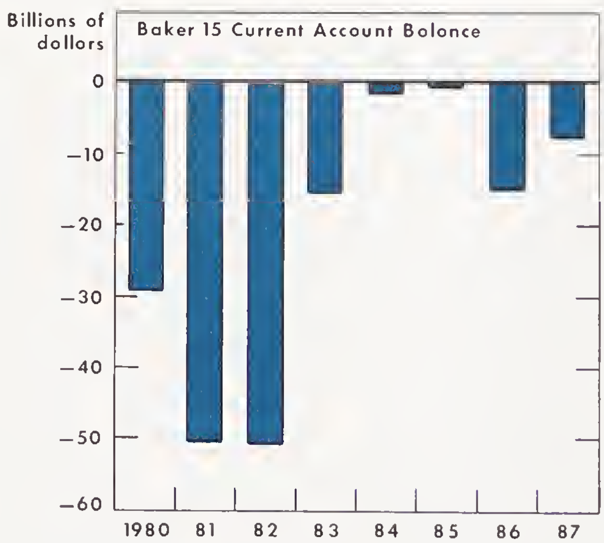
External adjustment has been a bright light for the LDCs. An impressive trade surplus . . .



. . . was generated mostly by compressing reliance on imports, . . .



. . . bringing near-balance in the current accounts.



Sources: IMF, Federal Reserve Bank of New York.

On its external accounts, however, Mexico's performance was even stronger than anticipated. In 1983 the country posted a $12 billion swing in its current account, to a $5 billion surplus, largely through a reduction of imports and a spurring of non-oil exports. The country replayed its strong performance the next year with a $4 billion current account surplus.

Marking Mexico's overall success, banks agreed to a new money package of $3.8 billion in early 1984. Loan spreads were reduced below those of a year earlier, to a range of 1 1/8-1 1/2 percentage points, and the maturities and grace periods were extended. In addition, the country and the banks agreed in principle in September on a MYRA covering $43.7 billion with lower spreads and longer maturities. This agreement had a number of novel features, including provisions to allow IMF monitoring of Mexico even after its Fund program had elapsed and options to permit non-U.S. banks to switch part of their exposure into nondollar currencies. The Mexican MYRA was not only a prime illustration of the evolutionary aspects of the prevailing debt strategy but also renewed evidence of the ability of debtors and creditors to work together in support of mutually beneficial results.

Like Mexico, Brazil made clear progress in 1983 and 1984. In February 1983, it devalued the cruzeiro by 23 percent against the U.S. dollar and undertook a three-year program supported by the IMF. The current account deficit improved sharply and the trade surplus jumped from $800 million in 1982 to $6.5 billion a year later. A surge in manufacturing exports the following year brought a small current account surplus. Strong export performance reversed three years of recession, with real growth of 5.7 percent recorded for 1984. In addition, the government took steps to reduce the fiscal deficit: subsidies were cut, particularly in the agricultural sector, the public sector wage bill was lowered by measures to reduce guaranteed increases in real wages, and public investment was reduced.

As in Mexico, inflation was the difficult aspect of adjustment. Despite policies to consolidate the budget system and control spending, the rate of inflation more than doubled between 1982 and 1984. Price pressures were in part a side-effect of a large depreciation and the cuts in subsidies. However, the growing monetary costs of servicing the inflation-indexed domestic debt of the public sector were a prominent factor behind the price rises, suggesting that inflation in the heavily indexed Brazilian economy had become self-reinforcing.

The course of the LDC debt crisis has never been uniform across countries. While Mexico and Brazil had their share of success in these early years, certain other countries were faring less well. In Argentina, for example, economic and financial problems predated the Mexican crisis and grew worse as the country passed through a political

sea-change that led to the collapse of the military government. Despite an extensive financial package in 1984, economic problems, particularly the growth of public spending, remained stubborn. Inflation soared, reaching close to 700 percent by year-end. Other debtor countries, too, were having a difficult time controlling public sector expenditures and inflationary pressures as 1985 approached. In Peru, the public sector deficits far exceeded targets and there, as in Nigeria, the Philippines, Uruguay, and Yugoslavia, price pressures were acute. While inflation troubled a number of Baker 15 countries, most took actions to address their problems and recorded substantial gains in their trade and current account balances in the early years of the crisis.

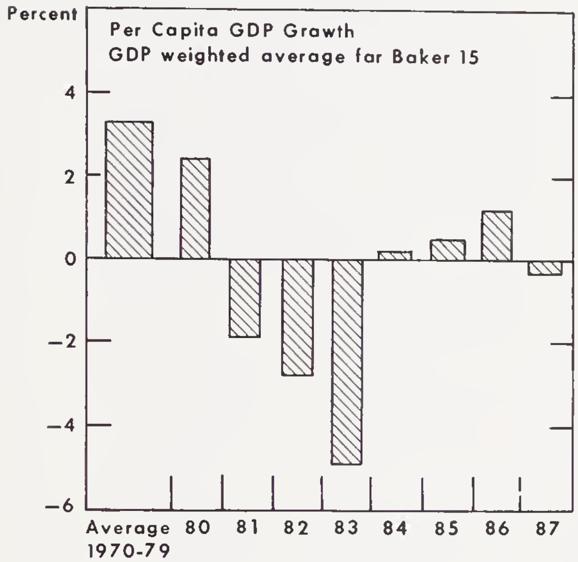
Despite the external improvements for Mexico, Brazil, and others, no Baker 15 country regained access to the international credit markets in these initial years: the restoration of creditworthiness, a continuing objective of the debt strategy, clearly would require a sustained commitment to sound policies of both a macroeconomic and structural nature. Many factors contributed to this state of affairs. None of the major debtor countries managed to control inflation, which appeared thoroughly entrenched. Such persistent high inflation raised the riskiness of financial investments in the debtor countries. The difficulties some debtors had in sustaining adjustment colored the market's perceptions of all potential borrowers, even the good performers. Finally, some international banks that had earlier participated in loan syndicates made strategic business decisions to withdraw from sovereign lending to LDCs. As 1985 unfolded, the stubborn features of the debt problem and the need for a long-term commitment to resolve them were all the more evident.

THE BAKER INITIATIVE

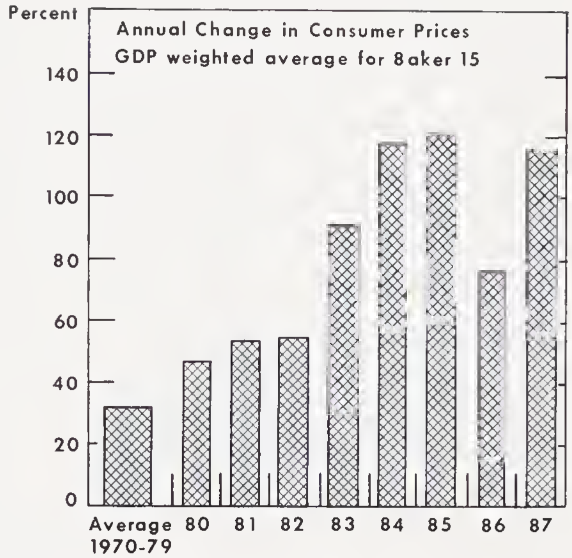
The first phase of the debt crisis had been a necessary period of reschedulings and adjustments in macroeconomic policy. The international financial system had functioned well through a period of enormous stress. While banks strengthened their balance sheets, debtor countries had started on the road to recovery. By the fall of 1985, however, it was clear that renewed momentum was needed (Chart 4). As the annual meeting of the IMF and the World Bank approached in the fall of 1985, the international community was keenly aware of the fact that the next phases of the LDC debt problem

Chart 4. LDC PERFORMANCE

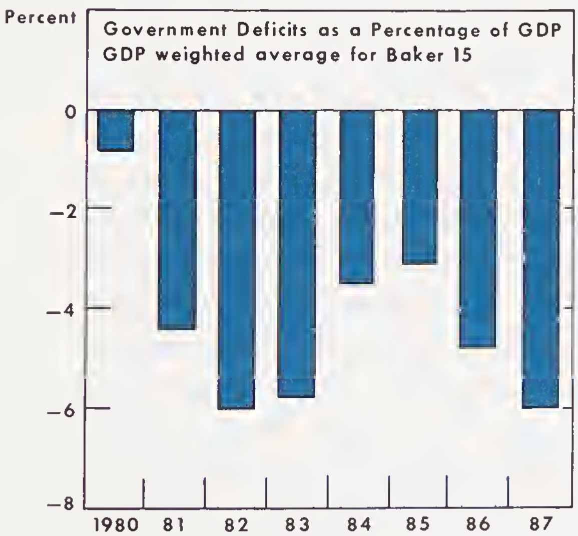
After a severe recession, debtor countries have had a limited measure of success restoring living standards, . . .



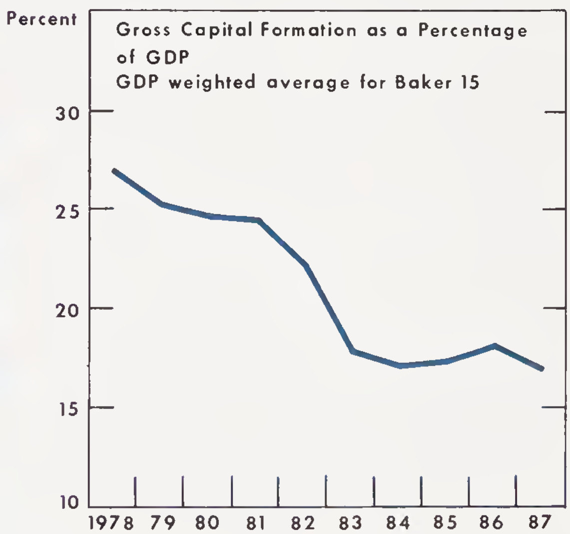
. . . but high inflation . . .



. . . and persistent internal deficits . . .



. . . have contributed to holding down investment.



Saurce: IMF.

would require some fresh thinking and initiative. What may not have been so apparent—at least with the benefit of hindsight—was just how much had been accomplished since the dark days of 1982, when the threat of an international economic and financial crisis was avoided.

Against this background, Secretary Baker proposed his initiative to move to a growth-oriented process, which meant, in part, undertaking structural reform in debtor economies to break down entrenched inefficiences. To ensure sufficient financing from both private and official sources to lubricate the whole process, the Secretary called on commercial banks to provide $20 billion in new loans over the following three years to the fifteen countries he identified as being most heavily in need. Further, to supplement bank finance, the Secretary called on the multilateral development banks, notably the World Bank, to increase their disbursements by $3 billion a year.

Economic and Structural Reform

After the Baker Plan was put forth, changes were taking place in the economic environment that would complicate the implementation of sound economic and structural reform policies. Average growth in the industrial world was slowing to under 3 percent. The boom in the United States had given way to a more sustainable expansion but no acceleration took place elsewhere in 1985 and 1986. The pattern of growth contributed to a sharp drop in non-oil commodity prices. Also, at the end of 1985, the OPEC price structure was breaking apart, leading to an unprecedented reduction in oil prices that exacerbated the problems of the oil-producing LDCs. The overall terms of trade moved sharply against the Baker 15. Lower inflation and interest rates in the industrial countries were not enough to offset the impact of the terms of trade decline. It became difficult in this environment for the debtor countries to sustain their improved trade picture while restoring some measure of economic growth.

In that general timespan, some positive developments were also taking place. Adjustment in Argentina, for example, seemed to be progressing. After a long spell of policy ineffectiveness and worsening creditor relations, the government had announced in June 1985 a shock program designed to halt the surging inflation rate. The plan included various fiscal actions, a wage and price freeze, the fixing of the exchange rate, and the

creation of a new currency unit, the austral. Inflation slowed dramatically to an annual rate of under 45 percent in the second half of 1985, and the public sector deficit fell. Growth resumed late in the year, and the external accounts improved sharply.

In early 1986, the freeze was lifted. Despite subsequent efforts to strengthen fiscal control, including several rounds of wage and price freezes, inflationary pressures and the fiscal deficit mounted sharply in 1987. Moreover, strong domestic demand, lower prices for major exports, crop losses due to bad weather, and tardy exchange rate adjustments sent the current account into a steep decline in 1986 and 1987.

The government turned to the IMF in 1987 and received a 15-month standby for SDR 1.1 billion in July. As part of the new program, the banks agreed to reschedule some $30 billion in debt and to provide Argentina with a new term-credit facility of $1.55 billion and $400 million of new trade credits. A novel aspect of the Argentine agreement was that it offered a range of options for participating banks. These included a bonus fee for early commitment to the package and an exit bond that would carry a lower yield than the bank loan but excuse the holder from future concerted lending.

Brazil introduced its shock plan, the Cruzado Plan, in February 1986 to deal with accelerating inflation of close to 250 percent. The Cruzado Plan fixed the exchange rate, created a new currency unit, ended most forms of indexation, and froze prices and wages, but only after a sharp wage increase. The initial wage increase combined with the price freeze led to a surge in domestic demand and an import boom that rapidly ate away at Brazil's trade surplus. Inflationary pressures, originally suppressed under the freeze, reemerged. Attempts toward the end of the year to stem the inflation failed, and price rises mounted to triple-digit levels in early 1987. In February 1987, as international reserves fell and economic growth slowed sharply, the government declared a moratorium on payment of interest on medium- and long-term debt. However, a major devaluation and the resumption of the use of a crawling peg to maintain the cruzado's competitiveness helped raise the trade surplus to $11.2 billion for the year. The moratorium disrupted the process of managing Brazil's debts, and by the turn of the year, the country was acting to restore relations with its creditors.

Mexico was among those battered by the collapse of oil prices in 1986. The Mexican economy went into recession that year, with domestic economic activity falling by 3.8 percent and inflation in triple digits. An aggressive exchange rate policy, which the country had initiated in mid-1985, helped to counter the impact of the oil price decline on overall economic activity. The exchange rate policy paid off in a gain of close to 40 percent in agricultural and manufactured exports, which together with some benefits from lower world interest rates, held the current account deficit in 1986 to roughly $1.3 billion. As domestic monetary conditions tightened, there was some repatriation

of flight capital in 1986. At the same time, the higher domestic interest rates led to sharp increases in the costs of servicing domestic debt and a rise in the public sector deficit to more than 16 percent of GDP. In November 1986, the Mexican government adopted a new economic stabilization program that was supported by an 18-month IMF standby of SDR 1.4 billion; the program called for the restructuring of official and bank debt, together with a new money package and more than $2 billion in net disbursements from the World Bank in 1986 and 1987.

The 1986 Mexican package was notable in several important respects. For one, the IMF arrangement included provision for additional finance should Mexico's oil prices fall below a floor level. Second, the bank agreement, which provided for new money of $6 billion, specified that $500 million of principal was to be guaranteed by the World Bank. Third, the bank agreement also allowed for additional financing under certain circumstances: $1.2 billion if a shortfall in Mexico's export receipts threatened the financing of the public sector investment program and $500 million, half guaranteed by the World Bank, if recovery failed to materialize according to a specified formula. This package, which integrated the World Bank more actively into a Fund financing package than ever before, provided Mexico with its lowest interest spread to date, 13/16 percent over LIBOR. The complex deal was another milestone in the process of designing increasingly sophisticated and flexible loan structures. But this complexity, together with concern about the oil market and greater creditor resistance generally, made for a drawn-out approval process.

Thereafter, the Mexican economy started to turn around. Following one quarter of negative growth, economic activity picked up by mid-1987, spurred by a firming in oil prices and record growth in manufactured exports. The country built its foreign exchange reserves up to $15 billion.

Mexico made strong gains, especially in restructuring its exports away from dependence on oil, but inflation remained a problem, as it did for many other LDCs. The growing fiscal deficit pushed inflation higher during 1987, up to an annual rate of nearly 160 percent by year-end. Late in the year, the government introduced a series of additional measures to stabilize the economy and curb inflation, including steps to speed up privatization and restructure public sector enterprises.

The Financing Process

In the years following the Baker initiative, international banks continued to reschedule debt extensively. In 1986-87, about $135 billion of bank debt was rescheduled for the Baker 15, about 50 percent of the total outstanding bank debt for the group. Terms and conditions negotiated were generally easier than those in the earlier round of reschedulings. Spreads were shaved to 13/16 of a percentage point for Mexico and Argentina and 7/8 of a percentage point for the Philippines, compared to a range of 1 1/8-1 7/8 percentage points for these countries in earlier reschedulings. Maturities were extended significantly, even out to 19-20 years in the cases of Argentina and Mexico . For a number of countries the reschedulings were of a multiyear character.

Assessing the overall performance of private net lending flows under the Baker initiative is more complicated, however. There were sometimes delays in reaching agreement on concerted lending packages. Still, two large packages—a total of $7.7 billion for Mexico and almost $2 billion for Argentina—were put together since 1985, as well as new facilities for other countries, such as Colombia, Ecuador, and Nigeria. International banks may have extended funds under concerted lending arrangements in the 1986-87 period in amounts somewhat below expectations, but the banks were responsive to the financing needs of those debtor countries that were implementing economic policy reforms and maintaining businesslike relations with creditors.

Outside of the concerted lending structure, changes were taking place on other fronts. Some private and public sector loans were repaid. In addition, many banks began exchanging claims for equity positions in the debtor countries and selling debt to nonfinancial companies that wanted to invest. Throughout the crisis, most banks maintained intact, or even increased, trade lines that continued to be serviced. Credits provided by nonbanks, however, showed a small decline on balance over 1986-87, even in terms of the dollar, which depreciated sharply during that period.

Concentrating on the flow of funds masks some interesting and important trends regarding the structure of financing. In general, both restructurings and new money packages have shown greater sophistication in design over the past two years. The so-called menu of options available to creditors has grown richer and includes such innovations as expanded choices for interest rate pricing, new cofinancing efforts with the official sector, exit bonds of one variety or another, as well as debt-equity conversions.

Some of these new techniques help to reduce the exposure of banks generally and promote in an orderly way the consolidation of claims into the hands of creditors who have long-term relationships with the countries. Mexico and Chile, for example, have

had particularly successful debt-equity programs that have reduced the stock of bank debt of each country by some $1.5 billion to $2.5 billion over the past two years. Many of the Baker Plan countries have, in fact, put debt-equity programs in place recently.

As another example, late in 1987, Mexico announced that it would offer creditor banks the chance to tender existing debt, at a discount from face value, against a new security carrying a higher yield and collateralized on its principal by U.S. government securities. In addition, the amount of debt successfully tendered would be excluded from the base for future new money commitments. The scheme was a modest success; Mexico accepted $3.7 billion of bank debt tendered, reducing its overall indebtedness by $1.1 billion.

Other techniques serve different purposes. Interest retiming, which allows for interest to be paid yearly instead of semiannually, was used in the rescheduling for Chile as a means to provide effective short-term financing without expanding new money commitments. The 1987 Argentina rescheduling offered a premium to banks that committed to the new money package before a specified time and was helpful in obtaining a quick agreement. The variety of these innovations illustrates the greater flexibility and imagination that has been brought to the financing process to the mutual benefit of debtors and creditors.

The Multilateral Institutions

The third element of the Baker strategy, beyond structural adjustment and growth and bank finance, was the role of the multilateral lending institutions. The call was for the World Bank, especially, to expand its lending to heavily indebted LDCs. This it has done to a large extent: commitments to the Baker 15 rose to about $13.0 billion in 1986-87 from $8.9 billion in 1981-82; disbursements increased to $11.3 billion from $5.2 billion in the same time frame (Chart 5).

The World Bank's efforts to adjust its programs and emphasis to the changing circumstances of the debtor countries have brought with them some important challenges for the Bank itself. For example, looming capital constraints have been exacerbated by the weakness of the dollar in the foreign exchange market, since the capital base of the

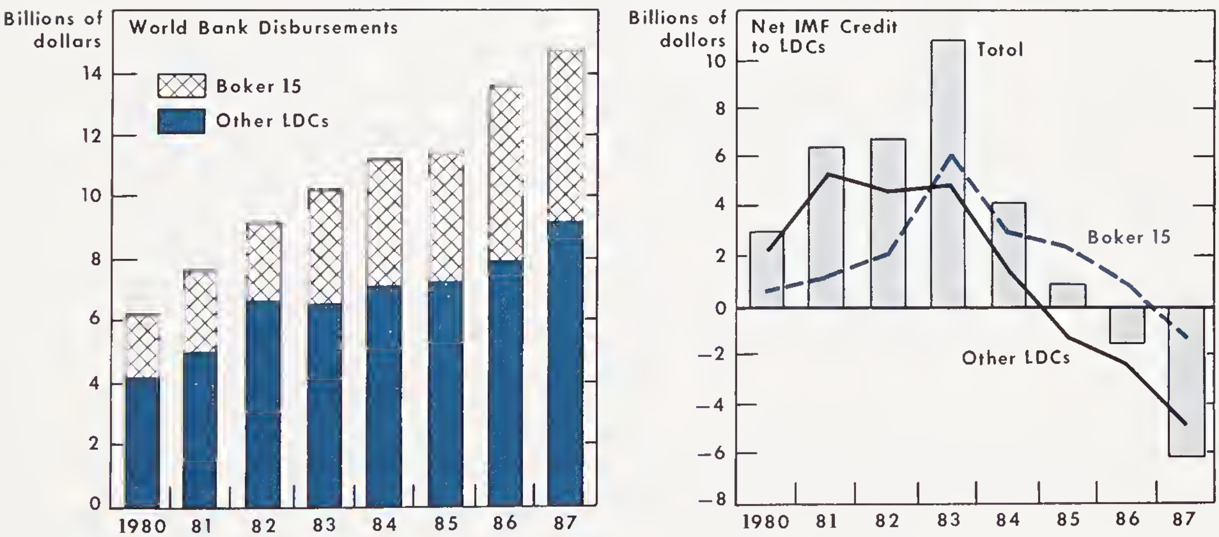
World Bank is denominated in dollars, but a significant portion of the institution's assets is held in nondollar currencies. Furthermore, the Bank has been cautious in its use of guarantees in cofinancing arrangements out of concern for jeopardizing its high credit rating and thereby raising its costs as a financial intermediary. For these reasons and, in addition, to enable the Bank to play the role envisioned for it in Secretary Baker's initiative, the World Bank is seeking from its member governments a substantial increase in its capital base.

Since the Baker initiative, the trend in net IMF credit has reversed its earlier direction. In 1983, net Fund credit to the Baker 15 totalled about $6 billion and was a significant buffer to the contraction of private finance. In 1986 and 1987, however, IMF credit net of repayments to these countries was declining. The Fund had extended substantial amounts earlier under traditional standby arrangements, which called for repayments in a medium-term time frame. The shift in the net flow of IMF resources was not

Chart 5. WORLD BANK AND IMF LENDING

As for the international institutions, the World Bank accelerated its disbursements . . .

. . . but net IMF credit went into reverse.



Sources: World Bonk, IMF.

widespread, however. If Brazil's repayment obligations are excluded, the IMF has on a net basis provided some \$1.5 billion to the Baker countries in 1986-87.

A central role for the Fund in the debt strategy remains crucial. The IMF is closely reviewing a number of possibilities for improving its effectiveness:

(1) modifications of its lending arrangements, to provide funds over a longer period and on a contingent basis to deal with fluctuations in the external environment;
(2) changes in the design of adjustment programs, to put a greater emphasis on structural adjustment policies;
(3) changes to streamline the use and number of performance criteria without undercutting the effectiveness of these criteria as a guide for adjustment.

A BALANCED APPROACH

Relative to the size of the problems that emerged in 1982, progress in addressing the debt crisis should be judged to be, on balance, encouraging. The approach that has evolved to deal with the crisis has proved to be flexible in adapting to the special circumstances of different debtor countries while upholding the general commitment of participants to the community of interests. This approach appeals to the enlightened self-interest of both debtors and creditors and works to their mutual advantage over the long run. It seeks a balance among the responsibilities of providing financing, undertaking policies of economic adjustment, and maintaining multilateral oversight and financial support of the whole process.

Experience over the years of the debt crisis has revealed the overall benefits of this basic approach. A major international financial crisis of global proportions was averted. Looking back on the initial stage of the crisis, it seems clear that resort to any course other than the one built on mutual self-interest would have risked serious conflict and disorder.

A balanced approach was appropriate for dealing not just with the immediate aftermath of the initial shock but also with developments over the longer term. The community of interests on which a balanced approach is based has endured rather well against the pressures and tensions it has faced. Certainly, there have been problems and setbacks,

but overall the basic commitments have remained intact. Dramatic but selective actions that challenged the cooperative balanced approach, such as payments stoppages or highly publicized provisioning, may have had a disproportionate effect on perceptions. However, behind those events, a good deal of quiet progress has been made on a number of fronts. The debtor countries as a group have preserved most of the improvements in their current account balances. Many countries have taken steps to begin the process of structural reform in their economies. New techniques in financing arrangements have promoted greater flexibility for creditors while achieving improved terms and conditions for debtors.

More remains to be done, however. Although positive growth rates have been restored in many countries, they are, by and large, still well below the potential increases in output that those economies can accommodate. Inflation has been widespread and persistent, and efforts to address it through macroeconomic policy and structural reform should be intensified. Delays in putting together financing arrangements have, at times, been too long; participants in the financing process must keep seeking new ways to increase its responsiveness.

Views may differ on the best tactics to deal with these difficulties while moving toward the basic goals of sustained growth, restored competitiveness, and reduced risk. A fundamental commitment to the community of interests, however, has to remain the keystone of future efforts to manage the debt problem. That basic strategy has a record of reasonably good performance and it is the only approach that treats the incentives for financing and adjustment in a balanced way.

Financial Statements

STATEMENT OF EARNINGS AND EXPENSES FOR THE CALENDAR YEARS 1987 AND 1986 (In dollars)

	1987	1986
Total current earnings	5,610,066,755	5,555,360,431
Net expenses*	171,855,794	212,628,002
Current net earnings	5,438,210,961	5,342,732,429
Additions to current net earnings:		
Profit on sales of United States government securites and Federal agency obligations (net)	13,476,274	21,891,327
Profit on foreign exchange (net)	434,830,746	486,745,710
All other	149,447	1,135
Total additions	448,456,467	508,638,172
Deductions from current net earnings	7,915,250	12,498,114
Net additions	440,541,217	496,140,058
Assessment by the Board of Governors:		
Board expenditures	20,642,300	24,112,100
Federal Reserve currency costs	53,905,512	53,649,878
Total assessments	74,547,812	77,761,978
Net earnings available for distribution	**5,804,204,366**	**5,761,110,509**
Distribution of net earnings:		
Dividends paid	30,455,531	27,204,022
Transferred to surplus	75,044,550	26,560,650
Payments to United States Treasury (interest on Federal Reserve notes)	5,698,704,285	5,707,345,837
Net earnings distributed	**5,804,204,366**	**5,761,110,509**
SURPLUS ACCOUNT		
Surplus—beginning of year	466,001,350	439,440,700
Transferred from net earnings	75,044,550	26,560,650
Surplus—end of year	**541,045,900**	**466,001,350**

*Includes a $49 million credit applied to expenses by the Federal Reserve Bank of New York on behalf of all twelve Reserve Banks, resulting from the implementation of FASB87—Employers' Accounting for Pensions—effective January 1987.

STATEMENT OF CONDITION

In dollars

Assets	DEC. 31, 1987	DEC. 31, 1986
Gold certificate account	3,177,290,421	3,145,946,460
Special drawing rights certificate account	1,489,000,000	1,489,000,000
Coin	16,279,966	14,120,224
Total	4,682,570,387	4,649,066,684
Advances	2,786,700,000	134,250,000
United States government securities:		
Bought outright*	70,429,481,550	64,078,918,598
Held under repurchase agreements	3,645,235,000	13,691,465,000
Federal agency obligations:		
Bought outright	2,430,086,784	2,538,623,843
Held under repurchase agreements	1,315,470,000	2,313,535,000
Total loans and securities	80,606,973,334	82,756,792,441
Other assets:		
Cash items in process of collection	934,827,927	1,311,198,153
Bank premises	33,425,781	32,247,470
All other†	3,444,024,737	4,378,765,998
Total other assets	4,412,278,445	5,722,211,621
Interdistrict settlement account	1,448,815,867	(5,576,252,155)
Total assets	**91,150,638,033**	**87,551,818,591**

*Includes securities loaned—fully secured	926,730,000	1,447,575,000

†Includes assets denominated in foreign currencies revalued monthly at market rates.

STATEMENT OF CONDITION

In dollars

Liabilities	DEC. 31, 1987	DEC. 31, 1986
Federal Reserve notes (net)	70,471,503,947	61,693,101,848
Reserve and other deposits:		
Depository institutions	11,652,719,955	14,639,122,344
United States Treasury—general account	5,312,879,052	7,587,759,178
Foreign—official accounts	130,344,855	173,759,073
Other	437,345,892	517,660,394
Total deposits	17,533,289,754	22,918,300,989
Other liabilities:		
Deferred availability cash items	875,600,715	1,157,759,287
All other*	1,188,151,817	850,653,767
Total other liabilities	2,063,752,532	2,008,413,054
Total Liabilities	**90,068,546,233**	**86,619,815,891**
Capital Accounts		
Capital paid in	541,045,900	466,001,350
Surplus	541,045,900	466,001,350
Total Capital Accounts	**1,082,091,800**	**932,002,700**
Total Liabilities and Capital Accounts	**91,150,638,033**	**87,551,818,591**

*Includes outstanding foreign exchange commitments valued at market rates.

Changes in Directors and Senior Officers

Peter Fousek, Executive Vice President and Director of Research, died on December 28, 1987. Mr. Fousek joined the Bank in 1950 and served in the Research and Foreign Functions before becoming the Vice President in charge of Personnel and the Bank's first Equal Opportunity Officer. He later returned to Research and Statistics as Economic Adviser and then Director of Research. In 1987 he also served as Associate Economist of the Federal Open Market Committee.

CHANGES IN DIRECTORS. In December 1987, the Board of Governors of the Federal Reserve System redesignated John R. Opel *Chairman* of the board of directors and *Federal Reserve Agent* for the year 1988. Mr. Opel, Chairman of the Executive Committee of International Business Machines Corporation, Armonk, N.Y., has been serving as a Class C director and as *Chairman* and *Federal Reserve Agent* since January 1987; in addition, he served as a Class B director of this Bank from January 1981 through December 1986.

Also in December, the Board of Governors appointed Ellen V. Futter a Class C director for a three-year term beginning January 1, 1988. As a Class C director, Ms. Futter, who is President of Barnard College, New York, N.Y., succeeded Virginia A. Dwyer, former Senior Vice President-Finance of American Telephone and Telegraph Company, New York, N.Y. Miss Dwyer had been serving as a Class C director since January 1985 and as *Deputy Chairman* since January 1987.

In December 1987, member banks in Group 3 elected J. Kirby Fowler a Class A director, and reelected John F. Welch, Jr. a Class B director, both for three-year terms beginning January 1, 1988. Mr. Fowler, President and chief executive officer of The Flemington National Bank, Flemington, N.J., succeeded Robert W. Moyer, President and chief executive officer of Wilber National Bank, Oneonta, N.Y., who had served as a Class A director since January 1985. Mr. Welch, Chairman of General Electric Company, Fairfield, Conn., has been serving as a Class B director since January 1985.

In February 1988, member banks in Group 1 elected John F. McGillicuddy a Class A director for the unexpired portion of the term, ending December 31, 1988, from which Lewis T. Preston had resigned. Mr. McGillicuddy is Chairman of Manufacturers Hanover Trust Company, New York, N.Y. Mr. Preston, who is Chairman of Morgan Guaranty Trust Company of New York, New York, N.Y., had served as a Class A director since January 1986.

Buffalo Branch. In December 1987, the board of directors of this Bank redesignated Mary Ann Lambertsen *Chairman* of the Branch board for the year 1988. Mrs. Lambertsen, Vice President-Human Resources of the Fisher-Price Division of The Quaker Oats Company, East Aurora, N.Y., has been a director of the Branch and *Chairman* of the Branch board since January 1986.

At the same time, the board of this Bank appointed Norman W. Sinclair a director of the Buffalo Branch for a three-year term beginning January 1, 1988. Mr. Sinclair, President and chief executive officer of Lockport Savings Bank, Lockport, N.Y., succeeded Ross B. Kenzie, Chairman of Goldome FSB, Buffalo, N.Y., who had served as a Branch director since January 1985.

Also in December, the Board of Governors of the Federal Reserve System appointed Paul McSweeney a director of the Buffalo Branch for a three-year term beginning January 1, 1988. Mr. McSweeney, Executive Vice President of the United Food and Commercial Workers District Union (Local 1), AFL-CIO, Buffalo, N.Y., succeeded Joseph Yantomasi, UAW Consultant, United Auto Workers, Buffalo, N.Y., who had served as a Branch director since January 1985.

CHANGES IN SENIOR OFFICERS. The following changes in official staff at the level of Vice President and above have occurred since the publication of the previous *Annual Report*:

Mary R. Clarkin, Vice President, resigned from the Bank effective September 11, 1987. Ms. Clarkin had joined the Bank's staff in 1960 and became an officer in 1975.

Effective October 1, 1987:

Suzanne Cutler, formerly Senior Vice President, was appointed Executive Vice President and assigned responsibility for the Operations Group.

James H. Oltman, formerly Executive Vice President and General Counsel, was designated Executive Vice President and Special Counsel and assigned senior oversight of the Accounting, Personnel, and Planning and Control Functions and of the new Funds and Securities Group. His assignment as the officer in charge of the Legal Function was terminated.

Ernest T. Patrikis, formerly Deputy General Counsel, was appointed Executive Vice President and General Counsel and assigned as the officer in charge of the Legal Function.

Frederick C. Schadrack, formerly Senior Vice President, was appointed Executive Vice President, continuing as the officer in charge of the Bank Supervision Group.

Stephen G. Thieke, formerly Senior Vice President, was appointed Executive Vice President and assigned as the officer in charge of the new Credit and Capital Markets Group.

The assignment of Chester B. Feldberg, Senior Vice President, to the Loans and Credits Function was terminated; his assignment to the Bank Supervision Group was continued.

Roberta J. Green, formerly Vice President, was appointed Senior Vice President, assigned senior oversight of the new Payments System Studies Staff, and designated as the officer in charge of the Loans and Credits Function.

Charles M. Lucas, formerly Vice President, was appointed Senior Vice President and assigned as the officer in charge of the International Capital Markets Staff.

Cathy E. Minehan, formerly Vice President, was appointed Senior Vice President and assigned as the officer in charge of the new Funds and Securities Group.

Robert M. Abplanalp, Vice President, formerly assigned to the Planning and Control Function, was assigned senior oversight of the Cash Processing and Check Processing Functions.

Carol W. Barrett, Vice President, was assigned supervisory responsibility for the Electronic Payments Function.

Joseph P. Botta, Vice President, formerly assigned to the Cash Processing Function, was assigned to the Automation and Electronic Payments Group with responsibility for the new Long-Range Planning Staff.

Ralph A. Cann, III, Vice President, was assigned senior oversight of the Accounting Function and the Planning and Control Function.

John M. Eighmy, Vice President, was assigned senior oversight of the Building Services Function and the Service Function.

Richard J. Gelson, Vice President, formerly assigned to the Statistics Function, was assigned as the officer in charge of the Accounting Function.

George R. Juncker, formerly Chief Compliance Examiner, was appointed Vice President and assigned as the officer in charge of the new Payments System Studies Staff.

Joan E. Lovett, formerly Assistant Vice President, was appointed Vice President and assigned supervisory responsibility for the Open Market Function.

Susan F. Moore, formerly Assistant Vice President, was appointed Vice President and assigned as the officer in charge of the Statistics Function.

Robert A. O'Sullivan, formerly Chief Financial Examiner, was appointed Vice President and assigned to the Bank Examinations Function.

William L. Rutledge, Vice President, was assigned to the Bank Examinations Function; his assignment to the Banking Applications Function was continued.

Barbara L. Walter, formerly Assistant Vice President, was appointed Vice President and assigned as the officer in charge of the Dealer Surveillance Function.

Betsy Buttrill White, formerly Assistant Vice President, was appointed Vice President and assigned to the Banking Studies and Analysis Function.

Herbert W. Whiteman, Jr., formerly Vice President, was designated Security Adviser, with responsibility for the Electronic Security and Security Control Staffs.

Effective December 1, 1987, A. Marshall Puckett, Payments System Adviser, retired. Mr. Puckett had joined the Bank's staff in 1963 and became an officer in 1967.

Effective January 1, 1988:

Thomas C. Baxter, Jr., formerly Counsel, was appointed Associate General Counsel.

Joyce E. Motylewski, formerly Counsel, was appointed Associate General Counsel.

Robert V. Murray, formerly Assistant Vice President, was appointed Vice President and assigned as the officer in charge of the Service Function.

Effective January 22, 1988, Richard G. Davis, formerly Senior Economic Adviser, was designated Senior Vice President and Director of Research and assigned as the officer in charge of the Research and Statistics Group.

FEDERAL ADVISORY COUNCIL. In January 1988, the board of directors of this Bank selected Willard C. Butcher and Thomas G. Labrecque to serve during the year 1988 as the member and alternate member, respectively, of the Federal Advisory Council from the Second Federal Reserve District. Mr. Butcher is Chairman of The Chase Manhattan Bank (National Association), New York, N.Y., and Mr. Labrecque is President of that bank. On the Council, Mr. Butcher succeeded John F. McGillicuddy, who was this District's member of the Council during 1986 and 1987.

Directors of the Federal Reserve Bank of New York

DIRECTORS

	Term expires Dec. 31	Class
JOHN F. MCGILLICUDDY Chairman of the Board, Manufacturers Hanover Trust Company, New York, N.Y.	1988	A
ALBERTO M. PARACCHINI Chairman of the Board and President, Banco de Ponce, Ponce, Puerto Rico	1989	A
J. KIRBY FOWLER President and Chief Executive Officer, The Flemington National Bank and Trust Company, Flemington, N.J.	1990	A
RICHARD L. GELB Chairman of the Board, Bristol-Myers Company, New York, N.Y.	1988	B
JOHN A. GEORGES Chairman of the Board, International Paper Company, Purchase, N.Y.	1989	B
JOHN F. WELCH, JR. Chairman of the Board, General Electric Company, Fairfield, Conn.	1990	B
JOHN BRADEMAS President, New York University, New York, N.Y.	1988	C
JOHN R. OPEL, *Chairman and Federal Reserve Agent* Chairman of the Executive Committee, International Business Machines Corporation, Armonk, N.Y.	1989	C
ELLEN V. FUTTER President, Barnard College, New York, N.Y.	1990	C

DIRECTORS—BUFFALO BRANCH

R. CARLOS CARBALLADA President and Chief Executive Officer, Central Trust Company, Rochester, N.Y.	1988
MARY ANN LAMBERTSEN, *Chairman* Vice President-Human Resources, Fisher-Price Division of The Quaker Oats Company, East Aurora, N.Y.	1988
DONALD I. WICKHAM President, Tri-Way Farms, Inc., Stanley, N.Y.	1988
MATTHEW AUGUSTINE President and Chief Executive Officer, Eltrex Industries, Inc., Rochester, N.Y.	1989
HARRY J. SULLIVAN President, Salamanca Trust Company, Salamanca, N.Y.	1989
PAUL MCSWEENEY Executive Vice President, United Food and Commercial Workers District Union (Local 1), AFL-CIO, Buffalo, N.Y.	1990
NORMAN W. SINCLAIR President and Chief Executive Officer, Lockport Savings Bank, Lockport, N.Y.	1990

MEMBER AND ALTERNATE MEMBER OF FEDERAL ADVISORY COUNCIL—1988

WILLARD C. BUTCHER, *Member*
Chairman of the Board, The Chase Manhattan Bank (National Association), New York, N.Y.

THOMAS G. LABRECQUE, *Alternate Member*
President, The Chase Manhattan Bank (National Association), New York, N.Y.

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